

SBA Information Notice

TO: All SBA Employees

CONTROL NO.: 9000-1703

SUBJECT: Fraud Involving SBAExpress
Loans

EFFECTIVE: 9/28/2007

This notice updates the Office of Inspector General's (OIG) 2006 alert about fraudulent schemes detected on a number of SBAExpress loans. The purpose of this notice is to prevent fraud by making you aware of patterns and indicators we continue to see in our investigations. Because we have noticed an increase in the number of potentially fraudulent SBAExpress loans, we ask that you forward this information to the immediate attention of lenders participating in your area, and that you ask all lenders to maintain a high level of diligence to identify and thwart this type of criminal activity. As a reminder, 13 C.F.R. § 120.197 **requires** lenders, Certified Development Companies, and others to notify the SBA Office of Inspector General "of any information which indicates that fraud may have occurred in connection with a 7(a) or 504 loan."

The perpetrators in SBAExpress fraud schemes have been borrowers and/or loan agents. Loan agents include packagers (who prepare loan paperwork for a fee) and referral agents (brokers who link prospective borrowers with prospective lenders). The same person may perform both roles. If an agent receives compensation from a borrower or a lender, SBA Form 159¹ must be completed by the borrower, the agent, and the lender.

Some of the patterns and indicators we are seeing in these schemes include the following:

- 1) A loan agent often recruits prospective borrowers through newspaper ads or in person at community organizations. The borrowers may be of the same ethnic group and are often recent immigrants. The agent submits the borrower's loan application package to the lender by fax or Internet, instead of in person. If a loan agent is identified in the documents, the agent's business address can be the same as that of a loan applicant, but with a different suite number.
- 2) Frequently the borrower or loan agent may check "no" to the question on the loan application that asks if a "packager" was paid to prepare the loan application. The loan package is instead termed a "referral."
- 3) Multiple loan applications are submitted *simultaneously* to different lenders for the same borrower. The borrower checks "no" to the question on the application that asks if he/she *previously* applied for SBA loans. Immediate relatives of the borrower submit loan applications as well. The loan agent will be the point of contact for more than one borrower and may use different names, but the phone number is often the same.

¹ See [http://yes.sba.gov/bigfiles/forms/informs/Form-159\(7a\).doc](http://yes.sba.gov/bigfiles/forms/informs/Form-159(7a).doc)

- 4) Multiple loan applications often reflect the same handwriting and business address. The borrowers have multiple fictitious business names for the same business or a slight variation of the business. Loans are obtained through various lenders for each fictitious business name. Fictitious financial statements are presented, but are usually dated well after the business' supposed start-up date, often within a few weeks of applying for loans.
- 5) Perpetrators also make false statements as to how long a business has been in existence, the number of employees, sales figures, the business address, and other information. In many cases, the businesses simply do not exist. This includes newly created or reinstated corporate entities that may exist on paper only.
- 6) Borrowers either use false Social Security numbers (SSNs) or obtain multiple loans through the same SSN. The same financial statements and bank statements are used for multiple businesses. The OIG has observed that financial documents submitted as part of one application have matched those submitted for another application, strongly indicating the financial and bank statements have been created and altered by the same person or group.
- 7) Borrowers obtain credit cards in addition to the SBAExpress loans from the same lender and charge the credit cards to the maximum limit and do not pay them down.
- 8) Loan funds are deposited into business accounts, but then are used for non-business purposes. Some perpetrators deposit loan funds in a business account, allow automatic loan payments to be withdrawn, and leave enough money in the account to cover several months of payments prior to default. Because the loans do not default immediately, lenders can be lulled into a false sense of security.
- 9) If a representative of the lender performs a site visit, the business site may be a rudimentary office space with a business name on the door. We also have noted instances in which the same product inventory has been used for different "businesses."

To deter and prevent this fraud, the OIG recommends that lenders take some or all of the following actions:

- 1) Monitor and track the involvement of loan agents in the loan application process.

Although a referral agent who receives compensation from either the borrower or the lender must be identified on SBA Form 159, a borrower may be under the mistaken impression that only a packager is required to be identified. A borrower often has a separate agreement with a referral agent to pay the loan agent a percentage of the loan amount once the loan is received. However, SBA Form 159 states that compensation charged to and that is paid by the borrower to an agent must bear a necessary and reasonable relationship to the services actually performed. *Moreover, compensation cannot be contingent on loan approval.*

SBA Form 1919², for SBAExpress, Community Express, and Patriot Express loans, was modified earlier this year to clarify that both packagers and referral agents are required to complete SBA Form 159. Even if the applicant checks “no” to Question No. 14 on Form 1919, be alert for “red flags” indicating possible loan agent involvement. For example, if the loan was “referred” to the lender by a third party, there must be a completed SBA Form 159 included with the application that is completed by the applicant and the referring agent. The referring agent may also be acting as a packager. The lender and SBA should know who all such individuals are. If there are red flags indicating that an agent may be involved, follow up by making sure that the borrower understands what a loan agent does and by asking whether any person has provided any type of assistance in preparing the application documents or in referring the borrow to the lender, whether the borrower is paying anyone a percentage of the loan or a fee for helping the borrower in any way to obtain a loan, and whether the compensation being required is within SBA’s rules as explained on SBA Form 159.

- 2) Verify the existence, location, and ownership of business borrowers through Dun and Bradstreet checks or other means, such as reviewing the state government’s secretary of state listings or conducting site visits. Our investigations have shown, for example, that fictitious businesses do not make the required tax filings with state departments of revenue or boards of equalization, nor do they file other tax returns. One useful tool is the Internal Revenue Service tax verification requirement in the SBAExpress Program Guide.
- 3) Make it a practice to conduct a site visit of the borrower’s place of business, and verify that the business is real and not just an office space with a business name on the door. Site visits should ascertain the legitimacy of a business and identify when a borrower is using a mail drop instead of a physical business location. Question whether the business plan and other documents make sense. In one case, a business supposedly grossed over \$1 million in sales. A site visit revealed the business was nothing more than a small room with a desk and a few carpet samples piled on the floor.
- 4) Ensure that multiple loans are not being made to the same borrowers or businesses or to businesses located at the same address. In several cases, the same SSN has been used to obtain loans from the same lender to different borrowers. Verifying that the borrower is on the lease for the rented space is one way of verifying the business’ legitimacy. If possible, screen SSNs to make sure that the number is not being used on more than one loan.
- 5) Try to make a positive identification of the borrower in accordance with U.S. Department of the Treasury requirements for customer identification programs.³ In one case, a lender

² See http://www.sba.gov/idc/groups/public/documents/sba_homepage/sba_form_1919patriotexpress.pdf

³ On May 9, 2003, the U.S. Department of Treasury and other agencies issued a Joint Final Rule (31 CFR Part 103) requiring various types of financial institutions to implement a Customer Identification Program (CIP). SBA subsequently required its lenders (including lenders other than banks) to have a CIP. (See Notices 5000--887 and 5000- 901.) For details on the Treasury rules, see <http://www.fincen.gov/326bankfinal.pdf> and <http://www.fincen.gov/finalciprule.pdf>.

accepted a photocopy of the borrower's driver license, which had been noticeably altered. Also, lenders should note that Section I of the checklist entitled Eligibility Information Required for SBAExpress Submission requires lender certification that the immigration status of the applicant has been verified.

- 6) Obtain full credit reports and question the borrower about any recent inquiries reflected on the reports. Such inquiries may indicate that the borrower is attempting to obtain multiple loans around the same time or has already obtained loans that he/she failed to disclose. Also, question the borrower about the lack of a credit history, as this may indicate that the borrower is using a fictitious name, business or SSN.
- 7) Monitor the business account to determine if the borrower is improperly using the loan funds.

If there are questions, or to report suspicious or potentially criminal conduct, contact the nearest OIG Investigations Division office (see <http://www.sba.gov/ig/hotline.html>).

Eric M. Thorson
Inspector General

Expires: 9/1/2008